

***United States Court of Appeals  
for the Second Circuit***



**APPENDIX**





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UNITED STATES COURT OF APPEALS

*for the*

SECOND CIRCUIT

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GEORGE J. SCHONHOLTZ,

Plaintiff-Appellant,

-against-

AMERICAN STOCK EXCHANGE INC., RAMSAY RE,  
FARRELL, ROCHLIN & ERDMAN and BEAR STEARNS  
& CO.,

Defendants-Respondents.

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE SOUTHERN DISTRICT OF NEW YORK

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JOINT APPENDIX

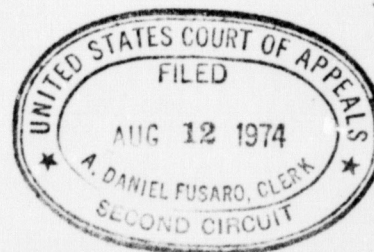
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SILVERMAN & HARNES  
Attorneys for Plaintiff-Appellant  
75 Rockefeller Plaza  
New York, N. Y. 10020

WINTHROP, STIMSON, PUTNAM & ROBERTS  
Attorneys for Defendant-Respondent  
Bear, Stearns & Co.  
40 Wall Street  
New York, N. Y. 10005

LORD, DAY & LORD  
Attorneys for Defendant-Respondent  
American Stock Exchange, Inc.  
25 Broadway  
New York, N. Y. 10004

(4235)



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## DOCKET ENTRIES

GEORGE J. SCHONHOLTZ vs AMERICAN STOCK EXCHANGE, INC. et al.

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73 CIV. 3689

DATE	PROCEEDINGS	Date Order Judgment No.
Aug 24-73	Filed complaint and issued summons.	
Sep 13-73	Filed summons and Marshals return on American Stock Exchange Inc., Ramsay, Re, Farrell, Rochlin & Erdman, by Mr. Peter C. & Sec. 8-28-73, and Bear Stearns & Co., 8-30-73.	
Oct 2-73	Filed stip and order extending deft. Ramsay, Re, Farrell, Rochlin & Erdman & Bear, Stearns & Co. time to answer until Nov. 12-73, & time for plff. to move for class action determination until Jan. 14-74. LASKER, J.	
Oct 4-73	Filed stip and order extending time for deft to answer until Oct. 25-73. LASKER, J.	
Nov 5-73	Filed stip and order extending time for deft. American Stock Exchange to answer until Nov. 28-73. LASKER, J.	
Nov 9-73	Filed stip. & order extending time for deft. Ramsay, etc. - to answer to 11-28-73- Lasker, J.	
Nov 27-73	Filed deft Bear, Stearns & Co. Notice of motion to dismiss the complaint. Ret. 12-7-73.	
Nov 27-73	Filed memo of law in support of motion.	
Nov 30-73	Filed defts notice of motion to dismiss complaint. Ret. 10-10-73.	
Nov 30-73	Filed deft American Stock Exchange memo in support of motion.	
Dec 4-73	Filed stip & order that motion of defts Ramsay, et al ret 12-7-73 is adjourned to 1-18-74, & motion of American Stock Exchange, ret. 12-10-73, is adjourned to 1-18-73. So Ordered, Lasker, J.	
Dec 9-74	Filed stip and order adjourning defts. motion until Feb. 8-74. LASKER, J.	
Jan 23-74	Filed plffs affdvt in opposition to motion to dismiss complaint.	
Feb 6-74	Filed plffs memo of law re dismissing complaint.	
Feb 6-74	Filed reply memorandum of deft. Amer. Stock Exchange in support of motion to dismiss	
Feb 8-74	Filed reply memorandum of law in support of defts' Ramsay re: motion to dismiss	
Feb 8-74	Filed affdvt. of Michael DiGiovanna re: Rule 9(f)	
Feb 26-74	<i>Pre-trial hearing held</i>	
May 6-74	Filed MEMO OPINION # 40679 *** We conclude pltf. has failed to state a Section 10(b) claim against any of the defts. Motions to dismiss are granted. So Ordered. LASKER, J. (n/m)	
May 31, 74	Filed Notice of Appeal of Pltff. from order of Judge Lasker dated May 6, 74. Mailed notices to Lord, Day & Lord; Winthrop Stimson, Putnam & Roberts. (CN 6-5-74)	
May 31-74	Filed notice of plffs attorneys of change of address.	



## SUMMONS

[Seal of Court]

COMPLAINT

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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(SAME TITLE)

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Plaintiff, by his attorneys, Silverman & Harnes, alleges upon information and belief as follows:

JURISDICTIONAL ALLEGATIONS

1. The jurisdiction of this Court is based upon the Securities Exchange Act of 1934 (Exchange Act), §§1 through 34, as amended (15 U.S.C. §78aa et seq.) and in particular upon §§6, 10b, 20 and 27 (15 U.S.C. §§78(f), (j), (t) and (aa)), Securities and Exchange Commission Rule 10b-5, (17 C.F.R. 240.10b-5) Rules 170 and 177 of the American Stock Exchange Rules of Board - Conduct of Business and the Constitution of the American Stock Exchange, Art. II, Sec. 2.

CLASS ACTION ALLEGATIONS PURSUANT TO CIVIL RULE 11a

2. (a) (i) Plaintiff sold short on August 4, 1971 and August 11, 1971 an aggregate of 200 shares of common stock of Levitz Furniture Corporation (Levitz). On August 17, 1971 plaintiff covered his short sales by purchasing shares of Levitz common stock at prices in excess of the short sale prices. The short sales and the covering transaction were executed through the facilities of defendant American Stock Exchange



COMPLAINT

Inc. (AMEX).

(ii) Defendant AMEX is registered with the Securities and Exchange Commission (SEC) as a national securities exchange pursuant to Section 6 of the Exchange Act (15 U.S.C. §78f). It is located at 86 Trinity Place, New York, New York.

(iii) Defendant Ramsay, Re, Farrell, Rochlin and Erdman (Ramsay Re) is a firm of specialists responsible for maintaining an orderly market in certain securities. From October 20, 1969 to August 24, 1971 Ramsay Re acted as the specialist for the common stock of Levitz.

(iv) Defendant Bear, Stearns & Co. (Bear Stearns) directly and indirectly controls Ramsay Re. It directly and indirectly induced the wrongful activity set forth herein.

(v) Plaintiff brings this action individually and representatively against defendants and on behalf of all other persons who purchased Levitz common stock on the AMEX during the period October 20, 1969 to August 24, 1971 in order to cover a short position.

(b) This action can be maintained as a class action pursuant to Rule 23 (b)(3) of the Federal Rules of Civil Procedure.

(c) The common stock of Levitz was listed, registered and traded on the AMEX. From at least October 20, 1969 to August 24, 1971, defendant Ramsay Re acted as the specialist in that stock.

COMPLAINT

The members of the class plaintiff seeks to represent are all persons who sold short common stock of Levitz and covered such short sales by purchase of Levitz common stock during the period October 20, 1969 to August 24, 1971.

(d) Plaintiff will fairly and adequately protect the interest of the class. His claim is typical of the claim which any class member could assert and his interest does not conflict with the interest of any other class member. The class is estimated to number many thousands of persons.

(e) Common questions of law and fact include (i) whether defendants maintained a fair and orderly market in Levitz common stock; (ii) whether there was sufficient Levitz common stock available "in the float" to meet the requirements of short sellers; (iii) whether a "float" insufficient to meet the requirements of short sellers in Levitz common stock developed which defendants knew, or in the exercise of the standards of care imposed upon them should have known; and (iv) whether the class sustained injuries as a result of any illegal or improper conduct engaged in by defendants.

(f) A class action is superior to other available methods because (i) the class members sustained relatively small losses and hence would have little interest in maintaining control of individual actions; (ii) to the best of plaintiff's knowledge, no member has as yet



COMPLAINT

commenced an action, so that a class action on behalf of such members will not deprive a class member of any rights; and (iii) there are no difficulties likely to be encountered in the maintenance of this suit as a class action.

SUBSTANTIVE ALLEGATIONS

4. During the relevant period, Levitz had 5,573,895 shares of its common stock issued and outstanding (as adjusted for a 2-for-1 stock split in June, 1971). Officers of Levitz, their relatives, and a partnership of which certain of the controlling persons of Levitz were partners, owned approximately 2 million of the aforesaid shares. Institutional investors such as investment companies registered with the SEC ("mutual funds"), banks, insurance companies and private hedge funds owned approximately 2.2 million shares. Thus, there was available to the investing public for trading approximately 1.3 million shares. The short interest in Levitz common stock was approximately 70,000 shares during the same period. Under all such circumstances, including the aforementioned substantial short interest, all of which defendants knew or should have known, the shares of Levitz common stock available for trading were inadequate to insure a fair, honest and orderly market in Levitz.

5. The AMEX represents and warrants to the public in its SEC registration statement, its constitution, rules and advertisements

COMPLAINT

that the securities listed and traded on its facilities are subject to rigorous scrutiny to insure that a fair, honest, and orderly market for such securities is maintained. In AMEX listed securities, the responsibility for maintaining an orderly market is shared by the AMEX and the specialist which the AMEX assigns to make a market in the Securities. The AMEX and the specialist have the responsibility to insure that members of the public can buy and sell securities at prices which are free from artificially inflated prices caused by a floating supply which is inadequate to meet the public demand.

6. Beginning at least on October 20, 1969 and continuing through August 24, 1971, the common stock of Levitz traded on the AMEX at artificially high prices created by a limited and inadequate supply of Levitz common stock. The fact of such limited and inadequate supply of Levitz common stock was or should have been known to defendants.

7. Plaintiff and the class were damaged when they covered their short positions in Levitz common stock by purchasing such stock at an artificially high price created by the inadequacy of the floating supply.

8. Defendants AMEX, Bear Stearns, and Ramsay Re knew or should have known that there was an inadequate supply of Levitz common stock, should not have allowed Levitz common stock to trade on



COMPLAINT

the AMEX at artificially inflated prices, and should have promptly suspended trading therein.

9. The AMEX and Bear, Stearns knew, or should have known, that Ramsay, Re was unable to maintain a fair and orderly market in Levitz common stock. By their failure to supervise Ramsey, Re in the performance of its duties as AMEX specialist in Levitz stock, defendants AMEX and Bear, Stearns aided and abetted, induced and contributed to the wrongful conduct complained of herein.

10. Had plaintiff and the class been adequately informed by the defendants of the material facts as to an inadequate floating supply of common stock, they would not have sold short.

WHEREFORE, plaintiff prays for judgment:

1. Declaring that this action can be maintained as a class suit;
2. Requiring defendants to pay to plaintiff and the class losses sustained;
3. Awarding plaintiff his costs and expenses, including accounting and legal fees; and
4. Granting such other and further relief as may be just and proper.

Dated: New York, N. Y.  
August 15, 1973

SACHS, GREENEBAUM & TAYLOR, Office & P. O. Address  
Of Counsel 1 Rockefeller Plaza  
1620 Eye St., N.W., New York, N. Y. 10020  
Washington, D. C. 20006

/s/ Silverman & Harnes  
SILVERMAN & HARNES,  
Attorneys for Plaintiff

NOTICE OF MOTION DATED NOVEMBER 27, 1973

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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(SAME TITLE)

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S I R S :

PLEASE TAKE NOTICE that upon the pleadings, the undersigned will move this Court in Room 2903 the United States Courthouse, Foley Square, New York, New York, on the 7th day of December, 1973, at 10:00 o'clock in the forenoon or as soon thereafter as counsel may be heard, pursuant to Rule 9 of the General Rules of this Court,

(a) for an order, pursuant to Rule 12(b)(1) of the Federal Rules of Civil Procedure, dismissing the complaint as to alleged defendant Ramsay, Re, Farrell, Rochlin & Erdman and defendant Bear, Stearns & Co. on the ground that the Court lacks jurisdiction over the subject matter of this action; and

(b) for such other and further relief as the Court may deem just and proper.

Dated: New York, New York  
November 27, 1973



NOTICE OF MOTION DATED NOVEMBER 27, 1973

WINTHROP, STIMSON, PUTNAM & ROBERTS

By /s/ John B. Daniels

A Member of the Firm

Attorneys for Defendant  
BEAR, STEARNS & CO.  
Office and P.O. Address  
40 Wall Street  
New York, New York 10005  
Tel. No. (212) WH-3-0700

TO:

SILVERMAN & HARNES  
Attorneys for Plaintiff  
One Rockefeller Plaza  
New York, New York 10020

LORD, DAY & LORD  
Attorneys for Defendant  
American Stock Exchange Inc.  
25 Broadway  
New York, New York 10004

NOTICE OF MOTION DATED NOVEMBER 28, 1973

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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(SAME TITLE)

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S I R S:

PLEASE TAKE NOTICE that upon the pleadings herein, the undersigned will move this Court before the Hon. Morris E. Lasker at Room No. 2903, United States Court House, Foley Square, New York, N. Y., on December 10, 1973, at 10:00 a.m., or as soon thereafter as counsel can be heard, or at such other time and place as the Court shall direct, for an order pursuant to Rule 12(b) of the Federal Rules of Civil Procedure, dismissing the complaint for lack of jurisdiction over the subject matter and failure to state a claim upon which relief can be granted, and for such other and further relief as is just and proper.

Dated: New York, N. Y.  
November 28, 1973

Yours, etc.

LORD, DAY & LORD

By /s/ John J. Toplin  
(A Member of the Firm)

TO: SILVERMAN & HARNES, ESQS.  
Attorneys for Plaintiff  
1 Rockefeller Plaza  
New York, N. Y.

Attorneys for Defendant  
American Stock Exchange, Inc.  
25 Broadway  
New York, N. Y. 10004



AFFIDAVIT OF SIDNEY B. SILVERMAN, FOR PLAINTIFF,  
IN OPPOSITION TO MOTION

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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(SAME TITLE)

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STATE OF NEW YORK       )  
                              :     ss.:  
COUNTY OF NEW YORK    )

SIDNEY B. SILVERMAN, being duly sworn, deposes and says:

I am a member of Silverman & Harnes, attorneys for plaintiff in the above entitled action. I submit this affidavit in opposition to the motion made by defendants for an order dismissing the complaint.

As reflected in plaintiff's memorandum of law submitted herewith, on motions to dismiss, such as the instant one, the allegations of the complaint are deemed to be true and every inference favorable to the validity of the claim should be drawn. For the Court's convenience, annexed hereto and marked Exhibit "A" is a copy of the complaint. In essence, the complaint charges that the defendants engaged in a trade, practice or course of conduct which amounted to a fraud and deception upon plaintiff and other members of the proposed class. Specifically, plaintiff sold short common stock of Levitz and covered such short sales during the period when Levitz stock was listed and traded upon

AFFIDAVIT OF SIDNEY B. SILVERMAN, FOR PLAINTIFF,  
IN OPPOSITION TO MOTION

the American Stock Exchange. Plaintiff contends that his covering transactions in Levitz stock were made at artificially high prices. Institutional interest in the stock had tied up a large portion of the floating supply. As a result, the price of Levitz stock was not at that time determined by free market conditions but was, rather, artificially inflated as a result of the inadequate quantity available to meet the demand of purchasers for that stock. Plaintiff charges that it was the duty of the defendants under rules enacted for the protection of investors, to maintain an orderly market in Levitz stock and that the failure to maintain such a market violates both the rules of the American Stock Exchange and the provisions of the Securities Exchange Act of 1934.

Defendants contend that plaintiff's action, if sustained, will open the flood gates to similar litigation based upon a disappointed investor's claim that an orderly market was not maintained. Defendants' argument is not pertinent to the instant situation. The short supply of Levitz common stock and the absence of an orderly market therein were the subject of review not only by the SEC, but also by the Attorney General of the State of New York. Exhibits "B" and "C" are examples of the attention given to the extraordinary circumstances that a corner may have developed in Levitz common stock. My review of reported decisions reflects that this case presents the first instance since the adoption of the Exchange Act that a charge has been made that a corner



AFFIDAVIT OF SIDNEY B. SILVERMAN, FOR PLAINTIFF,  
IN OPPOSITION TO MOTION

existed in a listed security. One case in 40 years hardly raises the spectre of a flood of litigation.

I believe that defendants' motion is ill-founded and should be denied. A review of the facts and pertinent authorities bearing thereon is contained in plaintiff's memorandum of law.

/s/ Sidney B. Silverman  
Sidney B. Silverman

Verified January 18, 1974.

FEB-2-1972

## FINANCE

# Check Finds Few Shares of Levitz Available to Trade

By ROBERT METZ

New York Times News Service

One of the biggest guessing games on Wall Street is estimating how many shares are in the Levitz Furniture Corp. "float" — shares actually available for trading on the New York Stock Exchange.

Clearly, a very substantial number of Levitz' 5,573,435 shares are closely held. The question some sophisticated investors are asking — the shorts as well as those who are long in the stock — is whether so many Levitz shares are locked up on the hands of a small group of large holders as to constitute a veritable corner on the stock.

(The opening of Levitz Furniture was formally delayed in opening on the New York Stock Exchange today by an influx of orders. The issue did not trade yesterday and on the previous day it declined 17 points to 137½. On that day, it was reported that the New York State attorney general's office was investigating mutual funds' role in sharp earlier gains in the issue.)

Just how many shares are there available for trading? It's anyone's guess, but here's one estimate pieced together by observers who have watched the stock. The Levitz family owns about 2 million shares. Mutual funds which report their holdings owned 1.3 million shares on Sept. 30. It is likely they owned more on Dec. 31, but the figures are not as yet available.

The Kaplan-Nathan & Co. hedge fund of which two Levitz brothers were, until recently at least, partners, owned 125,000 shares. Meanwhile, two leading New York City banks, held, according to a persistent rumor, 1.1 million Levitz shares. This could not be confirmed.

Street rumors have it that

other private hedge funds have 300,000 shares while another 300,000 shares are said to be in the hands of insurance companies.

Remember that many investment advisers to mutual funds also manage money in discretionary accounts and some also manage pension fund money. It's likely that they would buy shares of Levitz for their other accounts. Now figure that short covering would eat up about 99,000 shares and this leaves a free float of very few shares. Forget about the discretionary accounts and the pension funds and you have 5,573,435 minus perhaps 5,225,000 — if you believe the rumors — or about 350,000 shares.

When you figure the volume in Levitz, the float is about a five-day supply in terms of this week's trading.

How, then, can you have an orderly market with no supply and no way for a bear to go short. Meanwhile, the stock exchange has cancelled standing stop orders to sell at specified prices so that a seller must take the initiative to get out. But the exchange has not attempted to temper the volatile wide swings by putting in a 100 percent margin requirement.

Meanwhile, Merrill Lynch, Pierce, Fenner & Smith dropped its long-term buy recommendation today and now has no opinion on the stock.

2-1-72

1-31-72



## EXHIBIT C TO SILVERMAN AFFIDAVIT - NEWSPAPER ARTICLE

N. Y. Times

FEB 2 1972

**Market Place:** Levitz's 'Float': How Big Is It?

By ROBERT METZ

The biggest guessing game in town is estimating how many shares are in the Levitz Furniture Corporation's "float"—shares actually available for trading on the New York Stock Exchange.

Clearly, a very substantial number of Levitz's 5,573,435 shares are closely held. The question some sophisticated investors are asking—the shorts as well as those who are long—is whether so many Levitz shares are locked up in the hands of a small group of large holders as to constitute a veritable corner on the stock.

If you're one of the few investors who own Levitz shares—would you believe a recent \$40-million stock offering added only 300 or so to the 2,130 record holders who had owned the shares?—you no doubt know the Levitz furniture "concept."

The Levitz brothers have opened warehouse-salesrooms in a dozen states to sell furniture at a discount, but without, of course, the usual financial frills. So far there are 31 stores, with nine more under construction and more—many more—on the way, hopefully indicates Ralph Levitz, the ebullient chairman.

It's a high cash-flow operation since most customers do elect to lay it on the barrel and thus help provide the wherewithal for more inventory. New stores are financed through private investor groups and thus the company has relatively little debt.

Ralph Levitz brags that the company pays no dividends and thus the cash cost of equity financings are, as they

say, zip. The Levitz brothers and family took down some \$20-million of that recent \$40-million financing in selling personal shares. Many are asking pointed questions about the ability of the Levitzes to run more and more stores, especially since competition looms.

None of these considerations have cooled Wall Street's ardor and the stock has been a big winner with a 1971-72 high of 159 $\frac{1}{4}$ . Its low was 30 and a fraction. Trading halts recently have seen wide fluctuations and the stock was last traded on Monday. It closed with a 17-point loss at 137 $\frac{1}{2}$  after two trading halts and on a volume of 53,900 shares.

That same day, the Securities and Exchange Commission, the New York State Attorney General's office and the New York Stock Exchange all said they were investigating, but the company denied that any of them had contacted it yesterday.

Just how many shares are there available for trading? It's anyone's guess, but here's one estimate pieced together by observers who have watched the stock. The Levitz family owns about two million shares. Mutual funds that report their holdings owned 1.3 million shares on Sept. 30. It is likely they owned more on Dec. 31, but the figures are not as yet available.

The Kaplan-Nathan & Co. hedge fund of which two Levitz brothers were, until recently at least, partners, owned 125,000 shares. Meanwhile, two leading New York City banks held, according to a persistent rumor, 1.1 million Levitz shares. This could not be confirmed yesterday.

Street rumors have it that other private hedge funds have 300,000 shares while another 300,000 shares are said to be in the hands of insurance companies.

Remember that many investment advisers to mutual funds also manage money in discretionary accounts and some also manage pension-fund money. It's likely that they would buy shares of Levitz for their other accounts. Now figure that short covering would eat up about 99,000 shares and this leaves a free float of very few shares. Forget about the discretionary accounts and the pension funds and you have 5,573,435 minus perhaps 5,225,000—if you believe the rumors—or about 350,000 shares.

When you figure the volume in Levitz, the float is about a five-day supply in terms of this week's trading.

How, then, can you have an orderly market with no supply and no way for a bear to go short. Meanwhile, the stock exchange has canceled standing stop orders to sell at specified prices so that a seller must take the initiative to get out. But the exchange has not attempted to temper the volatile wide swings by putting in a 100 per cent margin requirement.

This would make the day trader put up the full cost of the shares rather than 55 per cent and might dampen the upswings. One short-trader asks: "Why don't they protect us the way they seem to be protecting those who are long the stock? Letting the market react without trading halts might also have a leveling effect." Shorts also complain that they couldn't borrow stock to increase their short positions.

Meanwhile, Merrill Lynch, Pierce, Fenner & Smith, dropped its long-term buy recommendation yesterday and now has no opinion.

JUDGE'S OPINION

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

-----X

GEORGE J. SCHONHOLTZ,

Plaintiff,

-against-

73 Civ. 3689

AMERICAN STOCK EXCHANGE INC.,  
RAMSAY, RE, FARRELL, ROCHLIN &  
ERDMAN and BEAR, STEARNS & CO.,

MEMORANDUM

Defendants.

-----X

APPEARANCES:

SILVERMAN & HARNES, ESQS.  
One Rockefeller Plaza  
New York, New York 10020  
Attorneys for Plaintiff

LORD, DAY & LORD, ESQS.  
25 Broadway  
New York, New York 10004  
Attorneys for Defendant AMERICAN STOCK EXCHANGE, INC.

WINTHROP, STIMSON, PUTNAM & ROBERTS, ESQS.  
40 Wall Street  
New York, New York 10005  
Attorneys for Defendant BEAR, STEARNS & CO.



JUDGE'S OPINION

LASKER, D.J.

In August, 1971, plaintiff sold short 200 shares of Levitz Corporation stock on the American Stock Exchange (Amex) and subsequently covered the sale at a substantial loss. He brings this action against Amex, the firm of Ramsay, Re, Farrell, Kachlin & Erdman (specialists in Levitz stock) (Ramsay) and Bear, Stearns & Co. (Bear, Stearns) Ramsay's parent. In substance the complaint <sup>that</sup> alleges/at the time of the events in question the common stock of Levitz traded on the Amex at "artificially high prices created by a limited and inadequate supply of Levitz common stock" (Paragraph 6); that this was known, or should have been known by defendants; and that plaintiff (and the class of short sellers of Levitz he seeks to represent) were damaged "when they covered their short positions ... by purchasing stock at an artificially high price created by the inadequacy of the floating supply." (Paragraph 7.) Plaintiff claims that defendants should "not have allowed" Levitz to trade at such artificially inflated prices and should have promptly suspended trading in the stock.

Jurisdiction is predicated upon §§6, 10(b), 20 and 27 of the Securities Exchange Act of 1934, 15 U.S.C. §§78(f), (j)(b)(t) and (aa), Rules 170 and 177 of the

JUDGE'S OPINION

American Stock Exchange Rules and the Amex Constitution. Defendants move pursuant to Rule 12(b), Federal Rules of Civil Procedure, 'to dismiss the complaint for failure to state a claim.

## I.

The motion to dismiss the §10(b) claims against all defendants is granted. Plaintiff charges that defendant Amex failed to supervise Ramsay in the discharge of Ramsay's obligation as a specialist, pursuant to Amex Rules, to "maintain a fair and orderly market," and that Amex, Ramsay, and Bear, Stearns (as controlling person of Ramsay) were under a duty to disclose that the market in Levitz stock was not in fact fair and orderly.

However, even taking these allegations as true, they do not state a §10(b) claim. Both Rule 9(b), Federal Rules of Civil Procedure, and decisions of this Circuit require that the circumstances constituting a §10(b) claim be stated with particularity and that merely conclusory allegations of fraud are insufficient to state a §10(b) claim. The present complaint fails those requirements. Plaintiff's claim boils down to the assertion that defendants impliedly represented to the public that there was an adequate floating supply of Levitz stock; that plaintiff relied on this representation; that the



JUDGE'S OPINION

floating supply was actually "inadequate" (Paragraph 8); that price movements in the stock were accentuated as a consequence; and that defendants were under a duty to disclose these facts and halt trading in the stock (Paragraph 8).

There exists no legal duty or rule of the Amex requiring disclosure of the fact that only 1.3 million shares of Levitz were available for public trading or indicating that such a lot is per se inadequate to assure an orderly market as contemplated by Rule 170. Exhibit D annexed to the Reply Memorandum of Amex sets forth the delisting policies of the Amex. The relevant section provides for delisting of a security where "(a) if the number of shares publicly held (exclusive of holdings of officers, directors, controlling shareholders or other family or concentrated holdings) is less than 150,000." Plaintiff's own allegations establish that the Amex complied with this policy. Rule 170 of the Amex, relating to the functions of specialists, (see Exhibit A, Amex Reply Memorandum) sets forth the general obligation of specialists "to engage in a course of dealings for his own account to assist in the maintenance, insofar as reasonably practicable, of a fair and orderly market." (emphasis added.) Other provisions of the rule detail

JUDGE'S OPINION

the kinds of transactions the specialist is either obligated to enter where practicable, in the performance of his duty, (such as dealing "for his own account in full lots when lack of price continuity or lack of depth in the full lot market exists...") or prohibited from entering (such as a purchase at a price above the last sale in the same trading session). Rule 177 provides that a specialist shall report to a floor official of the Amex any unusual activity or price change in a security, or material information regarding the issue or the market in it. The complaint alleges no violations of any of these specific duties. Even assuming the trading in Levitz stock was hectic or even dangerous, plaintiff points to no recognized legal duty on the part of any of defendants to disclose that fact, or any action or omission by defendants which amounted even to negligence, much less securities law fraud. See Shemtob v. Shearson, Hammill & Co., 448 F.2d 442 (2d Cir. 1971), Segal v. Gordon, 467 F.2d 602 (2d Cir. 1972). We conclude plaintiff has failed to state a §10(b) claim against any of the defendants.

## II.

Plaintiff's claims arising out of the alleged violations of exchange rules are also dismissed as to all



JUDGE'S OPINION

defendants. Even assuming that Amex rules were violated (although, as noted above, the complaint does not detail how), the few courts presented with the issue have held that violations of exchange rules are not per se actionable by private parties. In Colonial Realty Corp. v. Bache & Co., 358 F.2d 178, 182 (1966), Judge Friendly noted that violation of some exchange rules might provide the basis for a private cause of action "with the party urging the implication of a federal liability carrying a considerably heavier burden of persuasion than when the violation is of the statute or an SEC Regulation." In declining to imply a private cause of action for violation of §6 of the NYSE constitution providing for disciplinary action against members guilty "of conduct or proceeding inconsistent with just and equitable principles of trade," Judge Friendly noted the phrase was "something of a catch-all ... including merely unethical behavior which Congress could well not have intended to give rise to a legal claim," 358 F.2d at 182 and warned that "mere recitation of the statutory watchword by an aggrieved investor would saddle the federal courts with garden-variety customer-broker suits..." (358 F.2d at 183).

Judge Friendly's admonition has been taken

JUDGE'S OPINION

seriously by other courts presented with the same issue: no case of which we are aware has found an implied right of action for the violation per se of an exchange rule; allegations of such violation have been held to state a claim only where coupled with sufficient allegations of fraud on the investor. Buttrey v. Merrill, Lynch, Pierce, Fenner & Smith, 410 F.2d 135 (7th Cir. 1969), cert. denied 396 U.S. 838 (1969) (N.Y.S.E. Rule 405, the "know your customer rule," actionable in conjunction with allegations of fraud), Aetna Casualty & Surety Co. v. Paine, Webber, Jackson & Curtis, '69-'70 Transfer Binder, CCH Fed. Sec. L. Rep. ¶92,748 (N.D. Ill. 1970) (alleged violation of Rule 405 amounting to mere negligence failed to state a claim) accord, McMaster Hutchinson & Co. v. Rothschild & Co., 1972-73 Transfer Binder, CCH Fed. Sec. L. Rep. ¶93,541 (N.D. Ill. 1972); Bush v. Bruns Nordeman & Co., 1972-73 Transfer Binder, CCH Fed. Sec. L. Rep. ¶93,674 (S.D.N.Y. 1972) (alleged violations of Rule 405 "inextricably linked" with §10(b) claims stated a claim). These cases guide us here. Since we have found that plaintiff has failed to state a §10(b) claim, his allegations regarding violation of Amex rules, taken alone, do not state a claim.



JUDGE'S OPINION

The motions to dismiss are granted.

It is so ordered.

Dated: New York, New York  
May 6th, 1974.

MORRIS R. LASKY

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U.S.D.J.

NOTICE OF APPEAL

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

----- x

(SAME TITLE)

----- x

Notice is hereby given that George J. Schonblitz, plaintiff above named, hereby appeals to the United States Court of Appeals for the Second Circuit from the order of Hon. Morris E. Lasker, entered on the docket on May 6, 1974, granting defendants' motions to dismiss the complaint.

DATED: New York, N.Y.  
May 30, 1974

SILVERMAN & HARNES, ESQS.

By: SIDNEY B. SILVERMAN  
A Member of the Firm  
Attorneys for Plaintiff  
75 Rockefeller Plaza  
New York, New York 10019



Received 3 copies of the within

*Joint Appendix*  
this 12 day of Aug, 1974.

Sign James C. Menabone.

*Winthrop Stimson Putnam*  
For: 1 Roberts Esq(s).

Att'ys for Defendant Respondent  
Bear Stearns & Co.

Received 3 copies of the within

*Joint Appendix*  
this 12 day of Aug, 1974.

Sign Louis Barash

For: Ford Day & Ford Esq(s).

Att'ys for Defendant Respondent  
American Stock Exchange, Inc.